Dear Sens. Grassley and Baucus: The National Association of Manufacturers would like to submit the attached statement on the Tax Technical Corrections Act of 2006. Please contact me if you have any questions. Thank you in advance for considering our comments. Regards Dorothy Coleman

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Comments on the Tax Technical Corrections Bill of 2006 (S. 4026)

Submitted to the
Committee on Finance
U.S. Senate
By the
National Association of Manufacturers

October 30, 2006

Overview

The National Association of Manufacturers — the nation's largest industrial trade association — represents large, mid-size and small manufacturers in every industrial sector and in all 50 states. The NAM's mission is to enhance the competitiveness of manufacturers by shaping a legislative and regulatory environment conducive to U.S. economic growth and to increase understanding among policymakers, the media and the general public about the vital role of manufacturing to America's economic future and living standards.

NAM members applaud the efforts of the Committee to promote the pro-growth tax relief that is critical to the competitiveness of American manufacturers. Similarly, we appreciate the efforts of the Committee to advance legislation (S. 4026) that makes needed technical corrections to recent tax relief legislation.

In response to your request for comments on S. 4026, the NAM is extremely concerned about a provision (Section 7) included in the bill that would change the tax treatment of dividends paid from interest-charge Domestic International Sales Companies (IC DISCs). If enacted, this provision would make a substantive change in the current tax code, resulting in a tax increase on many privately-held manufacturing companies that export. As S. 4026 moves through the legislative process, we strongly urge you to drop Sec. 7 from the technical corrections bill.

Background

Continued export growth is critical to addressing our current trade deficit. While our trade deficit is large—on a seasonally adjusted basis, the August 2006 deficit in manufactured goods was at an annual rate of $536 billion—it has stayed at essentially the same range since January 2006. Export growth is stabilizing the balance. According to the Commerce Department, August 2006 was the 10th month in a row in which manufactured goods exports rose more rapidly than imports.

U.S. manufacturers play a major role in U.S. exports, exporting more than $60 billion in goods every month. In addition, exports from the United States have increased by 57 percent over the past ten years. <u>Nonetheless, in order for the manufactured goods trade imbalance to shrink, it is critical that export growth continue since import value is about 50 percent larger than manufactured goods exports value.</u>

While manufacturers of all sizes are exporters, the increase in exports by smaller companies has increased significantly in recent years. According to the Commerce Department, 97 percent of all exporting manufacturers have fewer than 500 employers. The NAM has tracked the exporting experience of smaller manufacturers for more than a decade. Based on a recent NAM survey, current export activity among smaller companies has doubled since 2001.

Potential Impact of Tax Law Change

If enacted, the proposed change in the tax treatment of IC-DISCs likely would have a negative impact on U.S. exports.

Under current tax rules, a U.S. manufacturing company that exports can set up a small IC-DISC that allows the deferral of taxes on certain income from export activities, as long as interest is paid on the deferred tax. In addition, when the income is distributed to noncorporate shareholders as a dividend, it is taxed at a 15 percent rate. The amount of deferral is capped at gross annual receipts of $10 million.

The proposed change in the IC-DISC rules would increase taxes for privately-held companies in the United States that export manufactured goods, making it more difficult for them to compete in the global marketplace. Roughly 90% of NAM's small and medium size companies (SMMs) —generally those with 1,000 or fewer employees—are privately held and many of these companies are exporters. In a recent survey of NAM's smaller members, more than two thirds of privately, family or individually owned companies responding to the survey said that they export products.

A Substantive Change

While the stated purpose of S. 4026 is to "make Congressional intent clear regarding crucial components of recent tax legislation, "Section 7 of the bill goes well beyond a clarification. Specifically Section 7 would significantly increase the tax rate on dividends paid by IC-DISCs, a substantive change to existing law, rather than a "technical correction."

Conclusion

In sum, the proposed changed to the IC-DISC rules in S. 4026 represents a substantive change to current tax law that would have a negative impact on the ability of some U.S. companies to export. Thank you in advance for considering our request to remove this anti-growth provision from the Technical Corrections Act of 2006. The NAM looks forward to continuing to work with Congress, the Administration and others to promote progrowth tax relief that encourages broad based economic growth and U.S. competitiveness.